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PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Telecommunications Division **RESOLUTION T-16656**
Market Structure Branch **May 16, 2002**

R E S O L U T I O N

RESOLUTION T-16656. VERIZON CALIFIORNIA, INC. (U-1002-C). ORDER ACCEPTING WITH MODIFICATION ADVICE LETTER FILING MADE IN COMPLIANCE WITH DECISION 98-10-026.

BY ADVICE LETTER NO. 9944 FILED ON DECMBER 12, 2001.

SUMMARY

This resolution accepts subject to future Commission order, Verizon California Inc.'s (Verizon) 2000 Rate of Return (ROR) adjusted for directory revenue and expenses from its supplemental 2000 sharable earnings advise letter (AL) 9944.

Since sharing has been suspended in Decision (D.) 98-10-026, there is no immediate impact on rates as a result of this filing.

BACKGROUND

New Regulatory Framework (NRF)

At the conclusion of the third triennial NRF review, the Commission issued D. 98-10-026, which suspended sharing effective January 1, 1999, continued the requirement for the reporting of rates of return, phased out existing Z factor adjustments and eliminated new Z factor adjustments, and included a provision for the consideration of only a very limited set of exogenous costs, and the continued rate caps and floors.

Pursuant to D. 98-10-026, Verizon filed its Annual Rate of Return advice letter for the purpose of reporting its rates of return and the market-based, benchmark, ceiling, and floor rates of return last found reasonable on April 2nd 2001. In Resolution T-16572 on October 25th 2001, the Commission approved Verizon's filing subject to any corrections or adjustments stemming from an upcoming NRF audit.

Pursuant to Ordering Paragraph 1 in resolution T-16572, Verizon submitted AL 9944 on December 12th 2001. Verizon reported that 11.39% was its revised intrastate ROR for 2000. Verizon also reported an estimated ROR of 13.96%, that reflects the inclusion of Yellow Page advertising revenue. Verizon states that the Yellow Page advertising revenue was included for information purposes only. Other references reported in Verizon's filing included the following rates of return:

Market-Based	10.50%
Ceiling	15.50%
Floor	7.75%

NOTICE/PROTESTS

Verizon states that the advice letter was mailed to interested parties on December 12, 2001. The Advise letter appeared on the Commission calendar January 4th 2002.

ORA sent in protest to AL 9944 on January 23, 2002. ORA protested, as they believe that Verizon is required to include directory revenues and expenses in its intrastate ROR. ORA disputes the qualifying footnote that the estimated ROR including directory-listing revenue is for information purposes only. ORA states that directory revenue and expenses have always been included above the line for ratemaking purposes. ORA contends that according to CPUC code, and NRF decisions directory revenue is to be used in calculating the utilities intrastate Results of operations and revenue requirements when setting rates for Category I, and Category II services.

ORA makes four recommendations regarding the advice letter.

1. ORA suggests that the approving resolution should affirm that Verizon is required to include directory revenues and expenses in its ROR, and strike the qualifying footnote.
2. ORA suggests that the Commission require Verizon to restate all monitoring reports that omitted directory revenue and expenses in their results of operations beginning with the year 2000.
3. ORA suggests that the Commission order Verizon to prospectively include an imputation adjustment to include directory revenue and expenses in all monitoring reports filed with the commission. The imputed adjustment will reflect the amount of revenue Verizon would have received had it not changed its contract with its publishing affiliate VIS.
4. ORA recommends that the resolution should state that the earnings statement remains subject to any adjustments found necessary as a result of future audits.

Verizon mailed a response on January 30, 2002, which disputed ORA's recommendations. Verizon claims that ORA's protest is "inconsistent with Commission precedent, seeks to prejudge the outcome of the 4th Triennial review of the New Regulatory Framework (NRF review), and seeks actions which are wasteful and unnecessary"

Verizon also argues that ORA's recommendation violates both Commission reporting requirements as set forth in D.91-07-056, and general accepted accounting principles. Verizon claims that D.91-07-056 states that earnings are to reflect each years operation as booked. Verizon also points out that the FCC has stated that yellow page revenues "may not be recorded on the carriers books"[1]. The FCC does not prohibit states from imputing revenues related to yellow page revenue for the purpose of state ratemaking, however, "states must exercise this authority without the use of part 32 accounts.

Verizon further contends that ORA's requested finding of fact would prejudge the outcome of the upcoming NRF review. Verizon points out that this issue is to be determined in Phase 3 of the NRF review.

Finally Verizon states that ORA's request for restatement of other monitoring reports is wasteful, and unnecessary. Verizon claims that by its count ORA's request could affect upwards of 30 quarterly, and monthly monitoring reports, some of which are submitted to other agencies, or are governed by FCC accounting policies. Verizon states that changing these reports would violate precedent and create confusion and complication, while presenting no new information.

DISCUSSION

Even though sharing has been suspended, the information reflected in the sharable earnings filing and other monitoring reports is a critical element of the NRF and is valuable to the Commission and other interested parties. The data contained in the affected reports may be used to support changes or reforms in the regulatory framework, or in evaluating a carrier's results of operations. Consequently, it is vitally important that Verizon report appropriate above-the-line operations for ratemaking purposes.

As ORA pointed out, the CPUC code is clear on the above the line treatment of directory revenues and expenses:

Public Utilities Code 728.2 (b)(1)

[1] Local Exchange Carriers' Permanent Cost Allocation Manuals for the separation of regulated and unregulated costs, AAD Nos 92-22 through 92-35, 9 FCC Rcd 4457(rel. August 29, 1994), para. 7

> The Commission's jurisdiction to regulate commercial advertising in alphabetical and classified directories of telephone corporations under this subdivision shall be limited to the rates and charges for commercial directory advertising, except that **the commission shall investigate and consider revenues and expenses of telephone corporations related to that advertising for purposes of establishing rates for other services offered by telephone corporations.**[2]

ORA is also correct that when the Commission adopted the NRF, directory revenues were included above the line. Since then no decision has relieved Verizon of this obligation.

Verizon's contention that including yellow page revenue in the intrastate rate of return would violate Commission and FCC precedent is incorrect. The FCC's own policy affords that "states may have the authority to impute revenues related to affiliate publishing of yellow pages directories for state ratemaking purposes."[3] Further, D. 91-07-056 states that the earnings calculations start with the Part 32 accounts less Parts 36 (separations), and 64 (below-the-line cost allocations) and allows "any modifications to those parts instituted by this commission." Traditionally, directory revenue has been included as one of these modifications. TD staff believes that an imputed amount for directory revenue should be included for purposes of calculating Verizon's intrastate rate of return until such a time as the Commission has relieved Verizon of this requirement.

Verizon's contention that finding directory revenues a required part of the intrastate ROR predetermines the outcome of the NRF review is incorrect. As directory revenue has always been a part of intrastate ROR, the Commission would be predetermining the outcome only if we did not include it.

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[2] Emphasis added

[3] Local Exchange Carriers' Permanent Cost Allocation Manuals for the Seperation of Regulated and Unregulated Costs, AAD Nos 92-22 through 92-35, 9 FCC Rcd 4457 (rel. Aug. 29, 1994), para. 7

We also agreed with ORA that it is inappropriate for a footnote to be included in the Intrastate Earnings Report that states the reporting of directory revenues and expenses is “for information purposes only”.

We are not persuaded by Verizon’s contention that restatement of other monitoring reports is unnecessary. To be effective monitoring reports must be complete. Therefore, Verizon should correct each of its monitoring reports which include California intrastate earnings as reported in the Intrastate Earnings Report to reflect an imputed earnings from directory operations. We direct Verizon to follow this reporting process going forward until Verizon is relieved of this obligation by a Commission order.

We believe Verizon AL# 9944 should be accepted subject to future Commission order.

FINDINGS

1. Advice Letter 9944 was filed in a timely manner.
2. It included an intrastate ROR, and an intrastate ROR adjusted for directory revenue.
3. The ROR adjusted for directory revenue was included estimated revenue had Verizon not changed its contract with its publishing affiliate VIS.
4. Confidential cost support was included in the filing.
5. A timely protest to this advice letter was filed by ORA.
6. Verizon filed a reply on January 30, 2002.
7. The Commission has always required Verizon to include directory revenues and expenses in its intrastate ROR.
8. Continuing to include directory revenues and expenses as an above the line contribution to Verizon's Results of Operations does not prejudge the outcome of NRF.
9. Verizon should include in its monitoring reports an imputed amount for directory operations equal to the amount it would have realized if the contract with VIS had not been modified.

10. Verizon's reported 2000 intrastate ROR is 13.96% and includes an imputed adjustment for directory revenue and expenses.
11. The qualification "for information purposes only" in note #3 in Verizon advice letter 9944 should be stricken.
12. Restatement of monitoring reports starting January 1, 2000, and prospective changes to future reports is appropriate.
13. The reference RORs are as follows:

- Market-Based – 10.5%
- Ceiling – 15.5%
- Floor – 7.75%

14. Sharing is currently suspended. Had there been sharing the calculated amount on the revised ROR would have been $0.

THEREFORE IT IS ORDERED THAT:

1. Verizon's revised 13.96% ROR is accepted subject to correction or adjustment pending future Commission order, and the phrase "for information purposes only" in note 3 of AL 9944 shall be stricken.
2. Verizon shall update all monitoring reports beginning January 1, 2000 to include an imputed adjustment for directory revenue to the California intrastate earnings. The imputed adjustment should reflect the revenue Verizon would have realized if the contract with VIS had not been modified.
3. Verizon shall include an imputed adjustment to include directory revenues and expenses in their California intrastate earnings until such a time as the Commission relives them of their responsibility to do so.

This Resolution is effective today.

I hereby certify that this Resolution was adopted by the Public Utilities Commission at its regular meeting on May 16, 2002 . The following Commissioners approved it:

WESLEY M. FRANKLIN
Executive Director